No. 20567

United States
COURT OF APPEALS
for the Ninth Circuit

ALONZO W. DERING,

Appellant,

v.

EVERETTE H. WILLIAMS, Trustee in Bankruptcy of Eldon P. Dering, bankrupt,

Appellee.

APPELLANT'S REPLY BRIEF

Appeal from the United States District Court for the District of Oregon

HONORABLE WILLIAM T. BEEKS, Judge

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REPLY TO APPELLEE'S STATEMENT OF FACTS

Appellee's Statement of Fact does not seriously controvert the Statement of Facts in Appellant's opening brief, but is incomplete and argumentative. Appellant believes it needs no reply.

SUMMARY OF REPLY ARGUMENT

1. Specification of Error No. 1

a) The four option documents dated December 6, 1961 to February 20, 1963, inclusive, as well as the agreement dated March 4, 1964 were what they purport to be.

b) The finding that such transactions were security devices is not supported by the evidence.

2. Specification of Error No. 2

The agreement of March 4, 1964 cannot be both a valid agreement and an invalid one.

If it is invalid as a transfer in fraud of creditors, when set aside, it reinstated previous agreements and the option of September 30, 1951 was in force and was exercised by appellant. If it was a security device, the option of September 30, 1951 was in effect. If it is valid, then appellee's rights were limited to the agreement. The District Court held that appellee was not entitled to recover under it because it had not been assumed by him (R. 49).

3. Specification of Error No. 3

The inconsistency of appellee's position is clearly evidenced by the assertions:

a) That the agreement of March 4, 1964 is invalid because it was a transfer without consideration and in fraud of creditors (Appellee Br. 21, 27, 28), and

b) That the same agreement of March 4, 1964 was valid, provided for cancellation of previous agreements and was "an agreement for sale or liquidation of the corporation" (Appellee Br. 9, 20).

Both statements cannot be correct. Analysis shows that the agreement was not in fraud of creditors. It was valid, but recovery was denied by the District Court on the ground that the trustee did not assume it.

REPLY TO ANSWER TO FIRST SPECIFICATION OF ERROR

Appellee asserts that appellant overlooked evidence in analyzing the option agreements, and the error committed by the Court in holding them to be security devices, but fails to point out any evidence not included by appellant.

Appellee also claims that the agreement of March 4, 1964 is not a security device within the purview of Finding No. 4 of the District Court (R. 88, Appellee Br. 12).

To avoid repetition, the appellant will reply to this contention in his Reply to the Answer to the Third Specification of Error.

Appellee cites *Umpqua Forest Industries* v. *Neenah Ore Land Co.* (1950) 188 Or. 605 at 633, 217 P.2d 219 at 230 (Appelle Br. 17), to the point that the debtor's pressing need for money puts him at the mercy of the creditor, which is a circumstance to "be considered as tending to show the intention to create a mortgage."

Appellant has no quarrel with this statement, but the evidence in the instant case does not show a "pressing need for money" at the time of the option of December 16, 1961, which fixed the character or status of the agreements (Tr. 14). Also, the transactions did not involve the insistent creditor, as transferee and optionor, which is the usual situation where a conveyance and option is claimed to be a security device.

Finding No. 4 holding these agreements to be security devices is inconsistent with the theory upon which appellee tried this case, and also is not supported by the facts. Amendments to the Pre-Trial Order will not be considered when the facts are insufficient.

REPLY TO ANSWER TO SECOND SPECIFICATION OF ERROR

Appellee challenges the timeliness of the exercise of the option of September 30, 1951 by appellant to purchase any stock interest in Dearing Industries, Inc., owned by the bankrupt or the trustee, as his successor.

A complete answer to this challenge is that the right to purchase under the option only became absolute upon bankrupt's adjudication, and it was exercised within a reasonable time thereafter.

Appellee also asserts that this option of September 30, 1951 was no longer in existence after the execution of the agreement of March 4, 1964 because it was cancelled by the latter agreement (Appellee Br. 20, 21). This claim that the agreement of March 4, 1964 was valid involves the same question as is raised in the

Answer to the First Specification of Error—the legal effect of the agreement of March 4, 1964. This will be fully covered by the Reply to the Answer to the Third Specification of Error.

REPLY TO ANSWER TO THIRD SPECIFICATION OF ERROR

Appellee asserts that the agreement of March 4, 1964 was within one year of bankruptcy and in fraud of creditors in that it released the equity of the bankrupt in the corporate stock of Dering Industries, Inc., without consideration except cancellation of indebtedness; that, therefore, the agreement is void and must be set aside.

This agreement was the only transaction between the parties within one year of bankruptcy. The District Court held that such a fraudulent transaction had occurred (Finding No. 6, R. 88), but was unable to identify the date of the transaction (R. 51). The appellee, in his attempt to sustain Finding No. 6, must pin the label on the agreement of March 4, 1964.

The entire agreement is as follows:

> "AGREEMENT—BETWEEN ALONZO W. DERING—ELDON P. DERING.
>
> "This agreement cancels the option dated February 20th, 1963 and signed by Alonzo W. Dering. This option was given to Eldon P. Dering for the purchase from Alonzo W. Dering of one hundred (100) shares of capital stock of Dering Industries, Inc. The purchase price for the purchase of such shares was to be the sum of ten thousand dollars

($10,000.00) plus accumulated interest at six percent (6%) from June 1, 1963 until date of purchase.

"This agreement is beingexecuted (sic) for the purpose of selling Dering Industries, Inc., or in the event that a sale is not made; to liquidate Dering Industries, Inc. This sale or liquidation to be started this date and be completed or in the process of completion by May 31st, 1964.

"It is agreed between Alonzo W. Dering and Eldon P. Dering that this agreement will be effective and neither party to this agreement can stop the proceedings once started.

"The proceeds from this sale or liquidation are to be divided as follows:

(1) Alonzo W. Dering is to receive one hundred dollars $100.00) per share for each share or capital stock of Dering Industries, Inc., held in his name at date of sale or liquidation.

(2) Eldon P. Dering agrees to purchase one hundred (100) shares of capital stock of Dering Industries, Inc., from Alonzo W. Dering for ten thousand dollars— ($10,-000.00) plus accumulated interest at six percent (6%) from June 1, 1963 to date of purchase. Date of purchase to be prior to date of sale or liquidation.

(3) Eldon P. Dering is to receive one hundred dollars ($100.00) per share for each share of capital stock of Dering Industries, Inc., held in his name at date of sale or liquidation.

(4) The profits from the sale or liquidation of Dering Industries, Inc., are to be divided equally.

"The intent of this agreement is to return twenty thousand dollars ($20,000) invested in Dering Industries, Inc., by Alonzo W. Dering as of this date plus interest at six percent (6%) on ten thousand dollars ($10,000.00) from June 1, 1963 until date of purchase of one hundred shares (100) of capital stock of Dering Industries, Inc., by Eldon P. Dering. This sale of stock by Alonzo W. Dering to Eldon P. Dering would make an investment of ten thousand dollars ($10,000.00) each by Alonzo W. Dering and Eldon P. Dering. The excess of over twenty thousand dollars—($20,00.00) to be equally divided between Alonzo W. Dering and Eldon P. Dering.

"This agreement, and all the terms thereof, is personal to Eldon P. Dering and Alonzo W. Dering and may not be sold, assigned, transferred or alienated, voluntarily or involuntary.

"Dated: March 4th, 1964."

The correct construction of this agreement is the most important point in this appeal.

1. Appellant contends the District Court committed error when the agreement, and the previous options, were held to be security devices. (First Specification of Error)

In answer, appellee says that this agreement is outside the scope of Finding No. 4 concerning security devices (R. 88).

2. Appellant contends that the District Court committed error when it refused to give effect to the option of September 30, 1951. (Second Specification of Error)

In answer, appellee says that this agreement of March 4, 1964 was valid and superseded all previous options which were held by the District Court to be security devices, and cancelled the option of September 30, 1951.

3. Appellant contends that the District Court found that there was a fraudulent transfer within one year of bankruptcy when there was no evidence of any such transfer. (Third Specification of Error)

In answer, appellee asserts that the agreement of March 4, 1964 was a fraudulent transfer and therefore voidable—although the District Court was unable to identify the transaction by date.

There are three possible constructions that can be put upon this agreement:

a) That it was a contract or option to buy and sell stock;

b) That it was a security device;

c) That it was a transfer in fraud of creditors.

Contract or Option to Buy and Sell Stock

This is the theory both parties adopted in the trial in the District Court. Appellant urged recovery should be denied because the trustee had not assumed the executory contract within the period of time allowed by

statute. Appellee asserted that adequate notice of assumption had been given, and that the provisions of the contract requiring concurrent performance by the bankrupt and the appellant were void as unenforceable (Contention No. 4, Pre-Trial Order, R. 38).

The District Court held that the appellee had not assumed the contract within the time required and therefore could not recover under its terms (R. 49).

Now appellee contends that this contract was valid to the extent that, by its terms, it superseded and cancelled all previous option agreements; that its provisions concerning the concurrent conditions are unenforceable (Appellee Br. 20, 21, 25, 26); appellee also contends that it was a transaction in fraud of creditors without fair consideration and must be set aside (Appellee Br. 21, 27, 28).

Appellant's position is that this agreement, as well as all previous agreements, was what it purported to be, and assigned as his First Specification of Error the holding by the District Court that these transactions were security devices.

Security Device

Appellee asserts that the agreement of March 4, 1964 was not held by the District Court to be a security transaction, claiming that Finding No. 4, which reads as follows:

> " '4. The various transactions involving the delivery and transfer of sums from defendant to bankrupt and from bankrupt to defendant and

> the execution and delivery of the aforementioned options superseded each other and said option documents were intended to constitute security devices for loans made by the defendant to the bankrupt.' (R. 88 Findings etc.)"

does not include the agreement of March 4, 1964 (Appellee Br. 13).

It is submitted the appellee's interpretation of Finding No. 4 is entirely too strict, since the finding includes transactions where no funds passed between the parties.

If the agreement of March 4, 1964 is not within the scope of Finding No. 4, there is no finding covering that transaction; it will be shown not to be a transfer in fraud of creditors; the District Court committed error in finding that the transaction was a security device, but having so found, committed additional error by not giving effect to the option agreement of September 30, 1951. This is the Second Specification of Error.

Transaction in Fraud of Creditors

In its Memorandum Opinion, the District Court found that there had been a transaction within one year of bankruptcy, otherwise unidentified, which was voidable because the only consideration therefor was the cancellation of indebtedness (Findings 6, 8; R. 88, 89).

Consideration for Agreement

Appellee asserts that the cancellation of the previous agreements ". . . was its sole objective *except for the apportionment of the proceeds.*" (Emphasis added) (Appellee Br. 24).

Since appellee admits that under the terms of the agreement, if bankrupt or appellee had assumed the contract and performed, certain moneys would have been payable to the bankrupt or the appellee, his successor in interest, the contention that the only consideration received by the bankrupt was the cancellation of an indebtedness must fail.

Appellee argues that the provision that the bankrupt was, by its terms, required to pay for such stock before May 31, 1963, and as a concurrent condition to its acquisition, was impossible of performance, would constitute a forfeiture and therefore was unenforceable.

If the provision as to concurrency of performance were held void, that would not destroy the consideration. However, the condition was not impossible of performance.

Whether insolvent or not, the owner of a contract right can borrow money upon it. If this right of the bankrupt was valued at $25,000, it would seem that $10,600 could have been borrowed against it.

There would have been some risk attached because Moncrief-Lenore might not have performed its executory contract. Appellee's plan apparently was to lay

back, let the appellant bear any risk of loss or litigation, and then, if everything went well, attempt to share the benefits. But if the benefits are to be shared, the risk must be shared. This the bankrupt and appellee were unwilling to do. In any event, appellant submits this question is moot, because the District Court found appellee had not assumed the contract (R. 49).

As additional consideration, however, the bankrupt was given approximately 85 days within which to exercise his rights under this agreement, whereas under the previous agreement he had only 15 days after demand within which to perform (R. 22, 23). This period of time extended well beyond the date of the trustee's appointment. Failure of the trustee to assume the agreement and perform does not destroy the consideration therefor or make the agreement in fraud of creditors.

Considering the foregoing, appellant submits that the Third Specification of Error, i.e., that there was no evidence of a transaction in fraud of creditors, must be sustained, since the evidence shows that this was not a transaction in fraud of creditors and admittedly was the only transaction between the parties within the year.

Effect of Avoidance of Agreement

It is submitted that if the transaction of March 4, 1964 is to be set aside, as being in fraud of creditors, then it must be set aside in its entirety. 11 U.S.C. 110 (e), Sec. 70(e) Bank. Act.

Apparently it is the appellee's position that the

transaction of March 4, 1964 is good and valid insofar as it cancels previous agreements, but still must be set aside as being in fraud of creditors:

> "The March 4, 1964, agreement specifically provides for the cancellation of the so-called option document of February 20, 1963. In view of the court's finding that the February 20, 1963 option document was a security device, it necessarily follows that the consideration which the bankrupt received for the sale of his equitable interest in the 100 shares of stock, worth $25,120 was simply a cancellation of his indebtedness of $10,600 . . ." (Appellee Br. 27-28)

Appellee does not explain how the agreement of March 4, 1964 can be set aside as a transaction in fraud of creditors, without reinstating the previous agreements, including the option of September 30, 1951.

The reverse is also true—if the agreement of March 4, 1964 was effective to cancel the previous agreements and as an apportionment of the proceeds, if the bankrupt, or the trustee as his successor, had performed, then it is not a transfer in fraud of creditors. Relief to appellee under this theory was denied because he did not assume the executory contract (R. 49).

CONCLUSION

1. The first question for decision is the status of the options of December 6, 1961; June 6, 1962; December 6, 1962 and February 20, 1963:

a) If these documents are what they purport to be,

bankrupt had no interest, legal or equitable, in any stock of Dering Industries, Inc.

b) If these documents were security devices, bankrupt had an equitable interest in stock in Dering Industries, Inc., subject to the option in favor of appellant dated September 30, 1951 which was exercised.

2. The second question for decision is the character of the agreement of March 4, 1964;

a) If the agreement of March 4, 1964 was what it purported to be, appellee had no right to recover because the District Court held appellee had not assumed the contract.

b) If the agreement of March 4, 1964 was a security device, appellant's rights under the option of September 30, 1951 continued and were exercised.

c) If the agreement of March 4, 1964 was voidable as a transfer without fair consideration, in fraud of creditors, it must be set aside in its entirety, the previous agreements reinstated and the rights of the parties determined in the light of the previous transactions.

In any event, the judgment in favor of appellee must be reversed. Whether or not appellee is entitled to recover a smaller sum from appellant depends upon this Court's decision on the "security device" question.

Respectfully submitted,

C. X. BOLLENBACK
Attorney for Appellant

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing brief is in full compliance with those rules.

C. X. BOLLENBACK